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C O N F I D E N T I A L SECTION 01 OF 02 CARACAS 001434

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USDOC FOR 4332 MAC/ITA/WH/JLAO

E.O. 12958: DECL: 11/03/2019
TAGS: ECON EFIN PGOV VE
SUBJECT: GBRV REDUCES REVENUE FLOWING TO THREE
OPPOSITION-CONTROLLED REGIONAL GOVERNMENTS

REF: A. CARACAS 503
¶B. CARACAS 1188
¶C. CARACAS 445
¶D. 2008 CARACAS 1453

Classified By: Economic Counselor Darnall Steuart for reasons 1.4 (b)
and (d).

¶1. (C) Summary: The Venezuelan government (GBRV) continues to find ways to reduce the funding provided by the central government to state and city governments, especially those run by opposition leaders. City officials in Maracaibo project their 2009 revenues will be 25 percent below what they initially estimated, largely as a result of GBRV-controlled entities stopping to pay or to collect taxes on Maracaibo's behalf. They believe the GBRV hopes to create a budget crisis in the city in the run-up to out-of-cycle elections for mayor expected in 2010. Separately, the law on the Metropolitan Area of Caracas completes a multi-step process by which the new government of the Capital District (whose head is appointed by President Chavez) gains and the state of Miranda and the Metropolitan Area of Caracas (both of which are currently led by elected opposition leaders) lose funding. These steps are indicative of what seems like a GBRV strategy to reduce progressively the financial capacity of public entities it does not directly control. End summary.

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Shortchanging Maracaibo Before an Election Year
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¶2. (C) In an October meeting, city officials from Maracaibo told Econoffs GBRV actions would cut 2009 revenue by 25 percent, or 155 million bolivars (Bs), below what they estimated at the beginning of 2009. (Note: Maracaibo is Venezuela's second largest city and is the capital of oil-rich Zulia state. At the official exchange rate of 2.15 Bs/USD, 155 million Bs equals 72 million USD. End note.) This reduction is largely due to actions by GBRV entities Enelven (Zulia's electric utility) and PDVSA (or joint ventures controlled by PDVSA). Enelven stopped its longstanding practice of collecting certain taxes on behalf of Maracaibo through monthly electric bills; PDVSA stopped transferring certain taxes it collects on the municipality's behalf; and Zulia-based joint ventures (JVs) stopped paying a certain type of royalty to Maracaibo. (Note: The GBRV recently changed the legal structure that governs how this royalty, which amounts to 3.3 percent of (the value of) the volume of oil extracted by the JVs and is known in Spanish as

"ventaja especial," is paid out. The changes reduce the amount going to municipalities and increase the amount going to entities controlled by the central government. Our understanding from the Maracaibo officials was that the Zulia-based JVs had stopped paying the "ventaja especial" owed to Maracaibo before this legal change. End note.)

¶3. (C) Maracaibo's Director General, Elias Mata (strictly protect throughout), said he believed the GBRV was deliberately seeking to create a budgetary crisis in Maracaibo in advance of a special election for mayor expected in the last half of 2010. (Note: Opposition leader Manuel Rosales was elected mayor in November 2008. The previous mayor was Chavista, and the actions by Enelven and PDVSA began after Rosales assumed office. Rosales subsequently fled Venezuela and successfully requested asylum in Peru in response to what he claimed were politically motivated corruption charges (ref A). A city council member from the same party as Rosales was designated interim mayor. End note.) In the face of the drop in revenue, Mata said the city was cutting back its investment budget and would end the year with significant unpaid labor liabilities. On the political front, he said the administration was communicating with city unions to explain the reasons the city could not cover all its liabilities to workers.

A Blow to Ledezma, a Jab at Capriles

¶4. (U) The new "Special Law on the Municipal Regimen in Two Levels for the Metropolitan Area of Caracas" (ref B), which went into effect in October, represents the culmination of a

complicated, multi-step process which, from a public finance perspective, channels income from Miranda state to the Metropolitan Area and channels income previously received by the Metropolitan Area to the newly created government of the Capital District (ref C), whose head is appointed by President Chavez. (Note: The Metropolitan Area is composed of five municipalities. Sixty percent of the population lives in Chavista-led Libertador municipality, which does not lie in any state and whose borders are synonymous with those of the Capital District. The other four municipalities, all headed by opposition mayors, lie in Miranda state. End note.)

¶5. (SBU) The law stipulates that Miranda transfer to the Metropolitan Area between 2.5 and seven percent of what Miranda receives from the "situado constitucional", a constitutionally-mandated transfer from the GBRV to state and local governments that constitutes the bulk of states' revenues (ref D). While significant to Miranda, this amount is far less than what the Metropolitan Area is losing to the Capital District. (Note: Previously, the Metropolitan Area received from the Central Government a "situado" transfer as if it were a state whose geographic boundaries were the same as Libertador's. This amount now goes to the Capital District. See ref B for more discussion of the impact on the Metropolitan Area's budget. End note.). As such, both Miranda state (currently governed by opposition leader Henrique Capriles Radonski) and the Metropolitan Area (currently governed by opposition leader Antonio Ledezma) lose funds to the new Capital District. In comments to the press, Capriles denounced the law as "political," an attempt to "pass the bill (for the Metropolitan Area) to the governor of Miranda, whereby the losers are the people (of Miranda)."

Comment

¶6. (C) The GBRV seems to be implementing a strategy of progressively reducing the real funding going from the central government to public entites not directly controlled by the GBRV. As far as other levels of government are

concerned, municipal governments are more shielded from the impact of this strategy, as the more developed municipalities receive the majority of their funding through local taxes. As Maracaibo's experience shows, however, they are still vulnerable. State governments, which cannot raise taxes and receive the vast majority of their income through constitutionally-mandated central government transfers, are far more vulnerable. The GBRV has already developed some mechanisms to change the amount and distribution of these transfers (ref D), and we have no doubt it will develop others. In the medium to long term, the cost to Venezuelan citizens will likely be very high, as municipal and state services suffer the impacts of limited or no investment. Given the complex public finance issues involved, it remains to be seen whether the public will assign the blame for these expected problems on President Chavez and the GBRV or on elected state and local officials. End comment.
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